

**ARIZONA PUBLIC SERVICE COMPANY'S RESPONSES TO ISSUES RELATING TO THE
ENVIRONMENTAL PORTFOLIO STANDARD
February 23, 2004**

As requested in the February 17, 2004 letter from Ray Williamson, APS submits the following comments to the identified issues relating to the Environmental Portfolio Standard ("EPS").

Issue 1: Increasing the EPS Funding Levels

The funding for the current EPS is not sufficient to permit affected utilities to actually meet the EPS goals on time. This was one of the conclusions of the Cost Evaluation Working Group ("CEWG") Report submitted to the Commission last year. Thus, increased funding should be established to accomplish the goals of the EPS.

For example, to actually achieve the current EPS goals, the funding for APS would need to be approximately \$50 million annually for the next four years, compared to the \$12.5 million that was available for the EPS in 2003. This figure assumes the existing program restrictions and substantiated estimates for future solar technology costs. Also, even with this higher funding, it may be after 2007 before the EPS goals could be met because of the time necessary to actually collect the funding and deploy the projects.

One method to allow for increased EPS funding is to modify the current EPS surcharge mechanism. Given the potential for changes in the estimated funding needs and costs associated with the EPS, a flexible surcharge mechanism may be the best method to provide for the necessary funding. These mechanisms could be developed in rate cases (such as the case pending for APS) where a cap on the total amount that could be collected in a given year could be established. That way, if costs needed for the program decline, the amounts collected by the surcharge could be reduced.

Issue 2: Elimination of the EPS Expiration Date

Eliminating the EPS expiration date will emphasize the ACC's commitment to renewables. However, periodic assessments of the EPS program (such as biennially) are still important to assess both continued progress in reducing the costs of renewable resources and to consider and facilitate potential improvements to the EPS program and ensure continued consumer benefit.

Issue 3: Restoration of DSM Funding

APS supports Ms. Keene's suggested approach, in the APS' rate case, where DSM funding is collected through a separate adjustment mechanism. DSM funding should be separate from the EPS funding, particularly since the current EPS funding is not

sufficient. The same process and attributes of an adjustment mechanism discussed above for the EPS could apply to a DSM adjustment mechanism.

Issue 4: Allocation of Funding Among Various Technologies

Due to significant differences in renewable technology costs and availability, changes in technology mix can have a significant effect on the cost of the EPS to consumers and on the ability of utilities to meet the EPS. Thus, if lower cost renewable resources were allowed to be a larger portion of a utility's EPS portfolio, the cost to meet the EPS would decline. Conversely, if the solar requirement increases, the cost to meet the EPS would increase as solar is more expensive than other renewable resources. If the Commission desires to meet or increase the portfolio percentages, changes in the allocation of funding among technologies is one method to accomplish that objective without significant cost increases.

Issue 5: Whether or not Arizona can and should increase its commitment to renewable energy by increasing the surcharge and the portfolio percentage.

Increasing the funding by increasing the surcharge will help utilities get closer to meeting the portfolio percentages of the EPS. Another way that the Commission could increase its commitment to renewable energy is to allow a lower-cost resource mix within the EPS. A lower-cost resource mix would allow program funding to go further and would make a higher portfolio percentage achievable. But, given the renewable resources available in Arizona, solar technologies undoubtedly would continue to be a major component of most utilities' EPS programs.

Issue 6: Review the requirements for the phase-in of renewable technologies as found in A.A.C. R14-2-1618.B.3. Review whether the approach of static percentages is still justified and if so, whether those percentages should be reconfigured.

As stated above, by opening up the standard to more technologies without static percentages, the EPS could achieve a higher portfolio percentage with a proportionally lower program cost.

Issue 7: Consideration of inclusion of new and emerging technologies as part of the review of the appropriate resource mix.

New or emerging technologies such as fuel cells could play a major role in Arizona's energy future. It is important to continually evaluate the role of new and emerging technologies in an appropriate resource mix, and the EPS should be broad enough to permit such resources to be included in the program.